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Agenda Item 3

August 15, 2011

TO: MEMBERS OF THE INVESTMENT COMMITTEE

- I. **SUBJECT:** June 2011 Policy Subcommittee Report
- II. **PROGRAM:** Total Fund
- III. **RECOMMENDATION:** That the Investment Committee approves:
 - a. Affiliate Fund Investment Policies
 - 1. Repeal of the Affiliate Funds Policy
 - 2. Adoption of the California Employers' Retiree Benefit Trust (CERBT) Policy
 - 3. Adoption of the Judges' Retirement System II (JRS II) Policy
 - 4. Adoption of the Legislators' Retirement System (LRS) Policy
 - 5. Adoption of the Long-Term Care Fund Policy
 - b. Global Equity – Revision of the Internally Managed Global Equity Index Funds Policy
 - c. Real Assets – Revision of the Infrastructure Program Policy
 - d. Adoption of the Role of Private Asset Class Board Investment Consultants Policy

IV. ANALYSIS:

The Policy Subcommittee met on June 15, 2011 to review the proposed repeal of the Affiliate Funds Policy and adoption of the California Employers' Retiree Benefit Trust (CERBT) Policy, the Judges' Retirement System II (JRS II) Policy, the Legislators' Retirement System (LRS) Policy and the Long-Term Care Fund Policy as related items. In addition, proposed revisions to the Internally Managed Global Equity Index Funds Policy and Infrastructure Program Policy and adoption of the Role of Private Asset Class Board Investment Consultants Policy were reviewed.

The repealed, revised and adopted policies are attached. Unless otherwise noted, the revised policies are presented as black-lined versions from the last adopted policy by the Investment Committee. The black-line uses strike-out to indicate deletions and double underline to indicate additions. Single underline

does not indicate a change; rather it indicates that the term is defined in the glossary.

Repeal of the Affiliate Funds Policy and Adoption of the California Employers' Retiree Benefit Trust (CERBT) Policy, the Judges' Retirement System II (JRS II) Policy, the Legislators' Retirement System (LRS) Policy and the Long-Term Care Fund Policy

The CalPERS Board administers the California Employers' Retiree Benefit Trust (CERBT) fund, the Judges' Retirement System II (JRS II) fund, the Legislators' Retirement System (LRS) fund and the Long-Term Care fund and manages separate investment policy portfolios for each fund. These funds are referred to collectively as the "Affiliate Funds." Adopted in 2008, the Statement of Investment Policy for the Affiliate Funds (Affiliate Policy) sets forth the overarching investment purposes and objectives. Individualized policy portfolio asset allocation targets and ranges for each of the Affiliate Funds are detailed in attachments to the Affiliate Policy. The Affiliate Policy was last revised December 2008 to achieve consistency among the Public Employees' Retirement Fund (PERF), CalPERS Supplemental Income Plans and Affiliate Fund policies.

Staff recommends repeal of the Affiliate Funds Policy and adoption of separate investment policies for each of the Affiliate Funds to eliminate confusion raised by members and employers when referencing this policy.

Based on recommendations provided at the meeting, Staff made the following changes:

- Amended Section II, C to read "maintain significant diversification to temper losses from market volatility."
- Amended Section III, B to read "CalPERS Investment Staff ("Staff") is responsible for the following:"

The Subcommittee recommends repeal of the Affiliate Funds Policy and adoption of the California Employers' Retiree Benefit Trust (CERBT) Policy, the Judges' Retirement System II (JRS II) Policy, the Legislators' Retirement System (LRS) Policy and the Long-Term Care Fund Policy.

Global Equity – Revision of the Internally Managed Global Equity Index Funds Policy

The Policy on Internally Managed Global Equity Index Funds sets forth overarching investment purposes and objectives with respect to all its investment

programs. Revisions to the policy identify the explicit range of the predicted tracking error for the Emerging Market Small-Cap strategy.

The Subcommittee recommends approval of the revised Policy on Internally Managed Global Equity Index Funds.

Real Assets – Revision of the Infrastructure Program Policy

In December 2010, the Investment Committee approved an alternative asset classification as part of the overall Strategic Asset Allocation process. The approval called for the creation of a new Real Assets classification comprised of the Real Estate program, and the Infrastructure and Forestland programs (previously part of the Inflation-Linked Asset Class).

In April 2011, the Committee approved a new Strategic Plan for Infrastructure. At the following meeting, the Committee adopted a single, overarching Real Assets Policy with attachments for the related investment programs. In response to this, Staff revised the Infrastructure Program Policy to reflect the approved Infrastructure Strategic Plan and Real Assets Policy provisions.

Black-lined and clean versions of the Infrastructure Program Policy are attached.

The Subcommittee recommends approval of the revised Infrastructure Program Policy.

Adoption of the Role of Private Asset Class Board Investment Consultants Policy

At prior Committee meetings, Staff was directed to explore the role of Private Asset Class Board Investment Consultants and explore the independence and economics surrounding consultant roles.

A preliminary discussion was held at the December 2010 Policy Subcommittee meeting and subsequently at the February 2011 Policy Subcommittee meeting. Staff presented the Private Asset Class Board Investment Consultant Policy as a first reading in April 2011 and a second reading in June 2011.

The Subcommittee recommends adoption of the Role of Private Asset Class Board Investment Consultants Policy.

V. STRATEGIC PLAN:

These items will further the following goals of CalPERS Strategic Plan:

- Goal I to exercise global leadership to ensure the sustainability of CalPERS pension and health benefit systems.
- Goal VIII to manage the risk and volatility of assets and liabilities to ensure sufficient funds are available, first, to pay benefits and second, to minimize and stabilize contributions.
- Goal IX to achieve long-term, sustainable, risk adjusted returns.

VI. RESULTS/COSTS:

The results of this item will provide CalPERS with enhanced efficiencies and ability to manage the overall portfolio. The revised policies will provide a foundation for compliance, accountability, and transparency.

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